BRANCH BANKING AMONG THE STATE BANKS

By H. M. P. Eckardt,
Saranac Lake, N. Y.

At the 1910 convention of the Alabama Bankers' Association, held in Birmingham in May, one of the speakers, whose topic was "State Banks and Their Branches," closed a condemnatory address with the words: "We believe the days of the branch bank are numbered." Two months later, at Cooperstown, Hon. E. B. Vreeland told the bankers of New York State, at their convention: "No one will ever live to see the day when the branch banking system which prevails in Canada and in Germany and in England and in France will be tolerated by the people of the United States."

I am sure that there are a considerable number of people in the various states whose opinions differ from those of the authorities I have quoted. Those who have closely followed the course of banking affairs must have noticed that the branch bank idea has made respectable progress. As is always the case when a reform struggles with hostile laws and against the opposition of established interests, it finds expression in a variety of ways. Thus, some bankers who desired to bring a number of banking institutions into cohesion have sought to attain their ends through purchasing the stock of other banks and controlling them through stock ownership. There are some cases wherein a practical banker has had himself elected or appointed to the presidency or management of a group of banks in a certain state or territory without his owning a majority of the shares of the several units. Then, the holding company method has been employed in some instances; and in a number of states small branch banks are operated under a sort of grudging toleration from the legislatures. It can be said that nowhere in the country are the branch institutions suffered to develop all the functions which they should exercise in order to attain their highest usefulness; nowhere is a branch bank allowed to develop to the dimensions that would fit it for taking care of a large part of the commerce and industry of a state or geographical division.

In his address to the New York State bankers, from which I

have already quoted, Hon. Mr. Vreeland said further: "The economies of the branch banking system are such that no other system can live beside it. It is just as sure as the sun will rise to-morrow that the branch banking system, if taken up in the United States, would in the end drive out of existence all the banks in every city and town in the country outside of the great financial centers. That is the experience of the world."

If this statement means anything it is a confession that the system of local single-office banks is wasteful in operation, and it seems to me that it sets forth one reason why branch banks are inevitable. When a banking system is wasteful it is the stockholders, borrowers and depositors who suffer from the circumstance, and as soon as they realize the fact its doom is sealed.

It should be said here that it is not their economical operation alone that has enabled the branch banks to displace the small local banks in England, Germany and France. The branch institutions are cleaner, more efficient, and they provide better opportunities for the clerks and officers; they give a better and more complete service to the localities in which they work. To illustrate this latter statement, I give the following comparison: In the United States at the present time it is not difficult to find cases like the following: There will be a town of say 2,500 or 3,000 people which has a little national bank or perhaps two of them. Surrounding this town at distances ranging from three to twenty miles are seven or eight small villages, the largest of which may have 1,000 or 1,200 population. Not one of these small places has a bank. The banks in the larger place at the center draw deposits from them all and perhaps do some discounting for a few of the principal business men in the outlying villages. Also, in the large town are a few manufacturing concerns which cannot get all the accommodation they need from the two local banks because the banks are too small. Consequently they are forced to borrow in New York or Boston.

If that locality were served by branch banks of the Canadian pattern there would be in the central town branches of perhaps three large institutions; and five or six of the outlying villages would be provided with branches or sub-branches. The manufacturers would borrow at home; they would not be compelled to go to New York or Boston. Everybody in any of these places, and the prosperous farmers in the tributary districts who possessed good char-

acter and a respectable standing, could borrow for legitimate needs. The country people would have excellent facilities for depositing in banks that had their confidence.

So it is because of the combination of economical operation and the provision of superior facilities, that the branch banks have crowded out the local banks in other countries. Another reason is found in their stability during crises. The stage coach has been superseded by the steam railway in America; and it is quite likely that for the very same reasons the local banks will in the course of time be obliged to give place to branch institutions. When the bankers get a clearer idea of the advantages that will accrue to them through the conversion of their single-office banks into branches, and when the people get a better conception of what properly constituted branch banks would do for them it is to be expected that progress in that direction will be accelerated.

In the meantime it is worth while to take note of the progress that has been made. Now it should be observed that mere size counts for much in the operation of branch banks. Large figures give prestige, and a widely spread system of branches makes for stability when the central administration is good. The different industries which the banks finance are not confined within the borders of particular states; and branch banking will never give the best account of itself while the operations of each bank are circumscribed by the boundaries of a particular state, no matter how large and populous the state may be.

However, we find that the federal laws are almost prohibitive. A newly organized national bank may not establish branches. In his article which appeared in the "Financier" of May 28th, 1910, Mr. W. J. Fowler, Deputy Comptroller of the Currency, says: "The operation of a branch by a national bank of primary organization, while not prohibited in expressed terms, is prohibited by implication, and the courts have held that what is implied is as effective as that which is expressed." When a state bank which operates branches is converted into a national bank it may continue to operate its branches under the national system, but presumably it may not open new branches or extend itself further in that manner. Mr. Fowler states that up to and including July 23d, 1908, there were but four instances of state banks with branches converting themselves into national banks and continuing to operate the branches.

The first conversion was on March 14th, 1907. It was that of a bank in Mississippi with $75,000 capital and one branch. The second state bank to convert also belonged to Mississippi. It had $50,000 capital and one branch. Conversion took place on May 31st, 1907; the branch was discontinued on February 6th, 1909, and the concern was placed in voluntary liquidation on April 1st, 1910. A third Mississippi state bank with $50,000 capital and one branch was converted on February 21st, 1908. The fourth conversion was that of an Oregon institution with capital of $50,000 and one branch. It occurred on July 23d, 1908.

On February 5th, 1910, the Bank of California, with capital of $4,000,000 and four branches, was converted into a national bank. This is the first instance of a branch bank of real importance operating under the national laws; and its course will be watched with great interest. Its capital and resources are large enough to give it prestige throughout the whole Pacific coast. If it and other banks were but permitted to open branches where they pleased and were suffered to operate them without being subjected to harassing taxes, prohibitions and restrictions, it is practically certain that they would rapidly enlarge their capitals and extend into hundreds of small places. The business men and small borrowers in those places might then expect to get accommodation at rates perhaps two-thirds as high as they at present pay to private banks and other small local institutions.

Among the state banks operating branches the Corn Exchange of New York occupies a prominent place. The New York State laws are not favorable to branch banking. Taxation is high and the stipulation that $100,000 capital shall be allotted to each branch is irksome. In other countries where the branch system is authorized and supported by the laws it is not attempted to regulate the capitalization of the branches. It would be impossible to do so. The balance due by the branch to the parent bank, or that due by the parent bank to the branch, fluctuates constantly in response to the operations of the bank's customers. Thus an important borrower at the branch may discount $300,000 worth of paper, and upon completing the advance the branch will owe head-office on balance $250,000. Then in due course the loan is paid off and some special deposits are received, with the result of throwing the balance on the other side—head-office may owe the branch $200,000. There

are many quiet localities where there is practically no demand for loans on discounts and where deposits constitute almost the whole business of the bank. For example, in a rich Eastern agricultural district a branch might have $600,000 or more deposits, and it may not be able to lend more than $50,000, no matter how earnestly the manager seeks for good borrowers. To force the parent bank to provide $100,000 capital for a branch of this type is an economic blunder. The branch already has over half a million of capital which it cannot use at home. When legislators pass laws of this kind they have in their minds the idea that the branch banks are merely contrivances for drawing the resources of the interior localities to the financial centers. So they create a set of conditions under which it is next to impossible for the banks to give good facilities to small places. It would be a wiser policy to encourage the establishment of sound banks in very small places and to supervise their head-offices so as to ensure that they provide properly and satisfactorily for the financial needs of the localities served by their branches. There are no means, other than through branch banks, of providing satisfactory facilities for small places. Doubtless because of the uncongeniality of the laws the Corn Exchange Bank has not spread its branches into the country districts. Its score of offices are found in the various districts of New York city.

Considerable interest attaches to the chain of one hundred or more state banks in Georgia which are combined under the one presidency. Apparently these institutions are held together merely by the fact that they have a common president. They represent what might be styled a banking federation. Each unit preserves its separate identity; and if the president were to resign or die presumably the federation might break up. There is in this arrangement a certain degree of cohesion between the parts, and it should be possible to transpose or transfer surplus funds from one part of the system to another when the occasion for doing so arose, just as the funds of a branch bank are thrown from one end of the system to the other in response to the demands of the industries and trades financed by the bank. But the tie in the Georgia case is personal. It is an instance of the one-man-power which is far too common in United States banking. In Canada it is the bank, and not the local manager, the general manager, or the president, that commands the fealty of the men. The bank has its history and traditions extending

back for fifty, sixty, or eighty years. The managers and presidents succeed each other while the bank grows and develops, spreading itself gradually into all the provinces and abroad into foreign countries. This great impersonal thing—the bank—is what the men serve. The best of them watch its progress from month to month and glory in its greatness.

So the Georgia aggregation can hardly be regarded as a branch bank. It is interesting, however, as an illustration of one method by which the branch bank idea is finding expression under discouraging laws. Last year in his annual report the Wisconsin Bank Commissioner registered a vigorous protest against the operations of a holding company in Minneapolis which had, he said, acquired control of more than forty banks in Wisconsin, Minnesota, and the Dakotas. One ground of objection was that these controlled banks proceeded to lend their funds to parties outside the state in which they were located. Of course there are serious objections to this method of doing business. But it is merely another illustration of how an irresistible force will break through or circumvent hostile laws. In the railroad and industrial worlds, capital has been allowed to concentrate itself and then, by means of agencies and branches, to diffuse its operations over huge territories. In time banking must be suffered to take the same course if the customers of the banks in the United States are to have the same advantages that bank customers in other countries enjoy.

Though it is objectionable in some respects, the Minneapolis holding company plan is preferable to that wherein one individual proceeds to acquire control over a number of banking institutions through purchasing a majority of the stock. There are two sets or cliques of great financiers in New York City credited with possessing control of chains of important banks in their own city and outside. When practised by financiers of a different grade, this method of concentrating banking capital may do considerable damage. Thus the activities of the Heinze-Morse group of financiers in acquiring control of other banks had something to do in precipitating the 1907 panic. Chains of banks formed after this fashion have no resemblance to properly constituted branch banks. Sometimes the financiers who form them do so with the object of enlarging the scope of their own borrowings. While the separate entity of each institution is preserved, there is no economy of administration and

operation such as is secured under the branch system. It merely means the extension of the domination of an individual or a set of individuals over a number of institutions, and the influence in question may often enough be of an undesirable or evil character.

In studying the banking development of the Western states one meets several phases of this process of individuals acquiring chains of banks. But in the West they call them strings rather than chains. Thus a news item may state that so and so of Blankville has bought a string of banks in the northern part of the state. This gives the idea that the transaction was somewhat similar to one involving the purchase of a drove of cattle or a number of barns and stables. Needless to say, such an aggregation of banks would not bear the slightest resemblance to the great branch banks of Canada, England, France, or Germany; and their operations cannot properly be regarded as branch banking among the state banks.

We now come to the consideration of the small branch institutions operating in a number of the states, which have very moderate capitals and only a few branches. In many cases these should be designated as local banks rather than branch banks; but, speaking technically, if a little concern of this description operates but one branch, it becomes a branch bank. Some of them appear to have been weak, struggling affairs which established one or two branches in near-by towns in the hope that the branches might be able to supply the parent bank with enough new deposit money to permit it to meet its obligations. Sometimes these so-called branch banks fail, and ruin and disaster come upon the hapless creditors who trusted them. These accidents also serve to bring branch banking into disrepute. The State of Alabama recently had some unpleasant experiences which led the president of the Bankers' Association to say:

It is with regret that I report that, growing out of the failure to carry out and enact into law the resolutions passed at Mobile, we have had a chain of bank failures in Alabama. Several Alabama communities have lost the savings of a lifetime . . . and all the banks have come more or less under suspicion. Your able ex-president, W. P. G. Harding, in his annual address at Mobile, said in substance: "While we have in this state some notable examples of the successful operation of branch banks, it appears that their success has been due entirely to the excellent character of the

management, and it seems imperative that we should have a law in Alabama regulating the establishment of branch banks in the future."

For all those who are interested in this subject of branch banking among the state banks, the report of proceedings of the Alabama bankers' 1910 meeting, as given in the New York "Financier," contains valuable data. I have not seen the question so exhaustively discussed in any other convention report. Although the Birmingham convention recorded itself in a condemnatory manner towards branch banking—probably for the reason that many of the examples of branch operation coming under the immediate observation of the members had not been calculated to win their admiration or respect—the arguments were not all turned in the one direction. Mr. S. S. Broadus, President of the Tennessee Valley Bank, gave a comprehensive and instructive description of the evolution of a single-office bank into a branch concern operating twelve offices. He related how he spent the year 1891 in the office of the Louisville Banking Company "studying how a great city bank is managed." Graduating from this school, he opened, in 1892, in Florence under the name of the Merchants Bank, and conducted the institution as a single-office bank for five years. In 1897 a branch was established at Tuscumbia, a county seat; then at Scottsboro, another county seat, and at intervals of a little over a year successive new branches were added to the system until in 1910 there were twelve branches besides the head or parent office. In 1908, the name of the bank was changed to Tennessee Valley Bank. The head office had been transferred from Florence to Decatur in 1904. The capital is $200,000. The following is said to have been the policy adopted in establishing branches:

> In locating our branch points I have never gone to places already having sufficient banking facilities, but generally to smaller points entirely lacking such. As a matter of fact, of our thirteen points not half of them could permanently sustain a small independent bank, while a branch of our large strong bank can take excellent care of the banking needs of a small community, which at the same time is a desirable part of the business as a whole.

Mr. Broadus' characterization of his $200,000 institution as "a large, strong bank" will perhaps bring a smile to the faces of bankers and others accustomed to the Canadian branch banks with capitals ranging from $2,000,000 to $14,000,000 and branch systems com-

prising from fifty to two hundred offices. But he means doubtless that his bank is large in comparison with the local institutions which it meets competitively in the small places of the Tennessee Valley.

In regard to stockholding, the management has aimed at having desirable business men at each branch point purchase a small interest in the institution; but a large holding by any one interest is not encouraged. To quote the president: "There is but the one corporation with stock in it owned by selected persons at our various points, some owning only one or two shares and seldom any more than ten. Then, at each point it is endeavored to have, from among the local shareholders, not less than one director." This latter policy would not be practicable in the case of a bank with numerous branches. For either the directors would be so merely in name, or the benefits attendant upon concentration of management would be largely lost.

One of the differences between branch banking and local banking is seen at once when the question of an office building comes up. Mr. Broadus says: "In opening a small branch bank I have always borne in mind that the influence of the local shareholders will naturally tend towards an expensive building 'to help the town.' For instance, they always urge a two-story building at least." If the bank is to be a commercial success its managers must fight against extravagance and waste just as the managers of other commercial ventures are obliged to do. The commercial and industrial development of a small locality is not usually permanently promoted by the erection there of a bank building more expensive than the bank can afford.

The staff is selected from country villages and no young men are employed who ever worked in a bank, because of the president's wish that they shall get their methods and inspiration from him. It is worth while noting here that the large Canadian branch banks draw their recruits to a large extent from country villages. They enter the bank at the age of seventeen or thereabouts and are trained in the bank's system and methods. The Canadian banks also import many youths from Scotland and England, because they cannot get enough juniors in Canada. They bring over juniors who are started at say $250 per year, and ledger men and clerks, not over twenty-three or twenty-four, with experience in bank work, and give them

$600 or $700. Both classes get regular increase of salary every year.

In the case of a small branch of a state bank it appears that the office will probably be started with but one man, and he perhaps taking charge fresh from his duties as clerk in a country store. In Canada no branches are started with less than two men, as the banks consider it absolutely necessary to have present in the office an employee other than the manager to serve as a check upon him.

The following account tells something of the method of reporting to head office used by the branches of the Tennessee Valley Bank, and it can perhaps be taken as applying to other well-conducted branch banks operating in country districts under state control:

> With the exception of a journal at each point, our books of original entry are put up in impression copy pads or in penwriter form. For instance, after the daily check and deposit record has been written up in full, the individual entries posted to the individual ledger, and the totals to the general ledger, the original sheets are carefully copied into an impression book, and then mailed to me at Decatur, reaching my desk next morning. Similarly as to a discount sheet at each branch point, this sheet showing any loans made during the day. A penwriter sheet sent daily to Decatur gives the items of all exchange drawn and all remittances made, and a daily balance with the branch.

An experienced banker will read between the lines here that these branches do not enjoy an extensive scope or freedom of action. The system would be in a better way of becoming popular throughout the country if the branch managers were trained men and possessed a larger degree of independence. It is one of the peculiarities of banking in the United States that a large numbr of bankers believe that a store clerk may be just as efficient as a branch manager as a trained professional would be and that a successful storekeeper, merchant, or manufacturer can undertake the active management of a bank as well as any other. Those ideas do not hold in the Dominion. There, banking is treated as a profession, and everybody who practises must pass through the various stages of a thorough education.

Under the Canadian system the branch managers are all trained men; also the local manager has a more dignified status in regard

to the matter of lending the bank's money. This is one of the most interesting parts of the whole subject. It is commonly urged by the opponents of branch banking that it is obnoxious to the business men of any locality to have their applications for loans passed upon by a far-away authority; and that the branch banks take the deposit money of the locality and send it away for use at other points, refusing to lend freely to local borrowers. In view of this argument it is interesting to observe what Mr. Broadus says about the practice of his bank. Under the heading "Making Loans," he remarks: "At first there is not much lending at our branch points, and at first it is all passed on by me. Later on small loans for less than $100 are made at our branch points without consulting me, such of course generally having more than one good signature or endorsement. In addition to small loans our branches make somewhat larger loans, but only along lines and to persons carefully considered and understood between our Decatur office and the branches. All of the more important lending is passed upon by me beforehand, the notes being run through at Decatur, even if it be but for $10 and only until pay day. . . . Our re-discounting during the summer time is altogether handled by our Decatur office, and is of course facilitated by our having the more important notes run through at Decatur as stated."

There is a wide difference between the operations of a branch of this kind and those of a newly opened office of a large Canadian bank. The Canadian manager starts to lend and discount at once. In fact that is the main part of his business except in the little towns and villages in quiet agricultural districts in Eastern Canada. The matter of the bank's having funds to lend for the regular business of local borrowers does not trouble him at all, scarcely even during periods of stringency. The only things he concerns himself about are the solvency and reliability of the borrower and the legitimacy of the transaction in which the bank's money is to be embarked. Provided the term of the loan is short, the manager of a good bank in a small place acts on his own responsibility in lending up to say $1,000. At a larger branch he would lend up to a higher figure. A credit of $1,000 covers fairly well all the requirements of the less important traders at a country village. For amounts exceeding that sum credits are applied for; and if the applicant is in a satisfactory position head-office will authorize the local manager

to take his paper up to an agreed-upon maximum, subject to certain rules and stipulations. Then the discounted paper is invariably held by the branch itself—if it is payable locally, and the Canadian banks do not rediscount. So if a borrower in a Canadian village goes to his bank with $500 to pay off his note a month ahead of its maturity the manager can always produce the note on the instant from the bill case. He does not have to ask the man to wait till he can get it back from head-office.

Deposits are a secondary consideration. Of course all branches strive to build up their deposit balances, as the deposits constitute the main source whence the funds for lending are derived. But the energies of the branch manager are mainly directed towards the acquisition of desirable discount accounts; and the bulk of the correspondence with head-office pertains to that department of the bank's business. It is found also that a policy of this kind results incidentally in the quickest development and growth of deposits. That is to say a branch that provides fully for the borrowing needs of the community in which it is located, at moderate rates, will usually be much more successful in building up its deposits than it would be if it starved the local borrowers and tried to develop the deposit department only.

In times of great stringency the regular customers of the branch get their credits from head-office very much as usual, but they are required to keep their borrowings within as small a compass as possible, and are discouraged from embarking in new ventures or extensions necessitating borrowed money. Also the branch manager is asked to refrain from canvassing or campaigning for important new discount accounts until the money situation relaxes.

From these remarks, it can be seen that branch banking as practised among the state banks is on a different basis from that prevailing in the Dominion. Except for one or two isolated examples it might almost be said that in the United States branch banking as it is understood in other countries is as yet scarcely existent. Under more favorable laws it would develop with surpassing rapidity; and it is quite probable that under the existing laws those branch banks which are now carefully and wisely developing themselves will evolve into institutions that will compare satisfactorily, in point of efficiency and usefulness, with the best branch banks of other countries.

There is no doubt that the small branch institutions in Alabama, Georgia, Tennessee, Florida, in the West and in the Eastern states, are providing valuable facilities. There is positively no method, other than branch banking, of giving the people who live in small villages and in remote country districts the banking facilities to which they are entitled and which they possess in other countries. The postal banks cannot provide them, since they are merely to accept limited balances on deposit and they are not to discount or lend. Where there is a private bank or small local bank in a little place of the kind to which I have referred it too often charges high rates of interest, especially in the West, and it may act the part of a money-lending shark.

Honorable Mr. Murray, the present Comptroller of the Currency, has done much during his tenure of office to improve the position of the national banks. He has stiffened up the bank examiners and caused the bank directors to take a closer interest in the affairs of their respective institutions. According to newspaper dispatches he is said to be engaged now in an effort to eliminate weak banks from the national system. His plans are thus outlined by the Washington correspondent of the Boston "Transcript:" "A bank," says the comptroller, "should go into voluntary liquidation as soon as it is demonstrated to a reasonable certainty that it cannot be continued successfully, or as soon as the examiner ascertains that the officers and directors cannot or will not manage its affairs in accordance with safe banking practice."

So, when a bank is found to be in this position, the bank comptroller directs that it be immediately placed in a satisfactory condition by the officers and directors then in charge; or that, if these officers and directors are unable to do so, a new element of strength must be brought into the bank, or, in other words, it must be placed under new management. Failing either of these developments, the officers and directors are urged to liquidate.

Few will dispute that for the comptroller to aim at the elimination of weak and unsafe banks is eminently laudable and proper. These banks are a menace to the whole country, and every year they inflict loss upon the people. But it is to be remembered that in many small places these weak banks constitute all that the community has in the way of banking facilities. If they are wiped out there will be nothing—at least nothing respectable—in the banking

line to take their places. Also it should be clear that under the present system there must always be hundreds and perhaps thousands of banks operating with inexpert management. An institution .tarting in a small place cannot usually command the services of a skilled manager, and the directors in most cases know nothing of banking. Under a good system in which branch banking was really encouraged excellent facilities would be provided for thousands of small places which now have none whatever and at the same time the management and direction at these small places would be of a high character.